No. 502

In the Supreme Court of the United States

OCTOBER TERM, 1957

CITIES SERVICE COMPANY, PETITIONER,

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

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In the Supreme Court of the United States

OCTOBER TERM, 1957

No. 602

CITIES SERVICE COMPANY, PETITIONER,

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the Court of Appeals is reported at 247 F. 2d 646 (App. 3a).[1] The Findings and Opinion and Order of the Securities and Exchange Commission ("Commission") are set forth in Holding Company Act Release No. 13254 (App. 19a).

JURISDICTION

The opinion of the Court of Appeals was entered July 15, 1957, and its judgment was entered on August

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[1] References to pages in the appendix filed by petitioner will be cited as "App. ——".

14, 1957 (App. 1a). The petition for a writ of certiorari was filed on November 8, 1957. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTE INVOLVED

Relevant provisions of the Public Utility Holding Company Act of 1935, 49 Stat. 803, 15 U.S.C. § 79, *et seq.*, are set forth in the appendix to the petition at pages 71a-72a.

QUESTION PRESENTED

Section 3(a) of the Public Utility Holding Company Act of 1935 authorizes the Commission to exempt a holding company from the requirements of the Act under certain conditions "unless and except insofar as it finds the exemption detrimental to the public interest or the interest of investors * * *" In the instant case, the Commission held that this proviso barred the exemption sought by petitioner, a registered holding company system, in view of the Commission's findings (*inter alia*) that the public minority stockholders of a subsidiary registered holding company are as a practical matter disenfranchised and that this disenfranchisement resulted in an "inequitable distribution of voting power" in violation of Section 11(b)(2) of the Act.

The question presented is whether the court below, in the particular circumstances of this case, erred in sustaining the Commission's denial of the exemption sought by petitioner.

STATEMENT

Petitioner, a holding company registered under the Public Utility Holding Company Act of 1935, seeks review of a judgment of the Court of Appeals for the

Second Circuit affirming an order of the Commission denying an application pursuant to Section 3(a)(5) requesting, on behalf of petitioner and its subsidiaries, an exemption from the provisions of the Act. The order was entered in consolidated proceedings involving (a) the exemption application and (b) an issue previously reserved by the Commission in proceedings under Section 11 of the Act concerning a 48.5% publicly held interest in the common stock of Arkansas Fuel Oil Corporation ("Fuel Oil"), a registered holding company subsidiary of petitioner (App. 21a).

The Commission found that the public minority interest in Fuel Oil constitutes a "complexity" and results in an unfair and inequitable distribution of voting power in violation of the standards of Section 11(b)(2) of the Act, precluding the grant of an exemption under the "unless and except" clause of Section 3(a), and that this condition could be rectified only by the elimination of the public minority interest or by petitioner's disposition of its interest in Fuel Oil (App. 46a). Accordingly, in an order entered on August 31, 1956, which was affirmed by the court below, the Commission denied the exemption (App. 47a). The Commission, however, withheld entry of an order under Section 11(b)(2) directing remedial action in order to afford the companies a reasonable opportunity to submit an appropriate program of compliance (App. 46a).[2]

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[2] Thereafter, on September 20, 1957, the Commission entered a Section 11(b)(2) order requiring such compliance (Holding Company Act Release No. 13549). Petitioner and Fuel Oil have filed petitions for review of that order in the Court of Appeals for the Third Circuit.

Background

In 1941, petitioner registered as a holding company under Section 5 of the Act, and it is still so registered [3] (App. 5a). It was the top company in a pyramided holding company system comprising 125 companies with extensive utility and non-utility interests and consolidated assets in excess of one billion dollars at December 31, 1941. The system included a number of registered public utility subholding company systems, both foreign and domestic, with consolidated utility assets of $439 million at the end of 1938.[4]

Reorganization of petitioner's system under Section 11(b) of the Act began in 1940 with the institution of proceedings against one of the system's subholding companies and was followed by proceedings against petitioner itself in 1941.[5] In 1944, the Commission, acting under Section 11(b)(1) of the Act,[6] ordered petitioner, which desired to retain its non-utility gas and oil interests, to divest itself of all its utility

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[3] A holding company is defined in Section 2(a)(7) of the Act as a company which directly or indirectly owns or controls 10 percent or more of the voting securities of a public utility company. A public utility company, as defined in Section 2(a)(5), means an electric or gas utility company. A registered holding company is defined in Section 2(a)(12) as a person, which includes a corporation (Section 2(a)(2)), whose registration is in effect under Section 5 of the Act.

[4] *Cities Service Company*, 15 S.E.C. 962, 964-965 (1944); 8 S.E.C. 318, 322 (1940).

[5] Holding Company Act Releases Nos. 1954 (March 4, 1940) and 2867 (July 3, 1941).

[6] Section 11(b)(1) requires that each registered holding company system be limited to a single integrated public utility system, with provision for the retention of additional utility systems and related incidental businesses under certain designated circumstances.

interests.[7] From 1940, more or less continuously until 1954, there followed numerous mergers, consolidations, dissolutions, reorganizations, and property divestments designed to bring the system into compliance with Sections 11(b)(1) and 11(b)(2). As a consequence of these various steps, petitioner now has one public utility subsidiary, a Canadian company, which it is required to dispose of (App. 24a).

One of the registered subholding companies in petitioner's system has been Arkansas Natural Gas Corporation ("Arknat"), the name of which was changed to Arkansas Fuel Oil Corporation ("Fuel Oil") (App. 53a). The principal subsidiaries of Arknat, which itself registered as a holding company in 1938,[8] were Arkansas Louisiana Gas Company ("Arkla"), a gas utility company, and Arkansas Fuel Oil Company ("Arkco"), a non-utility company (App. 51a).

In 1949 the Commission instituted proceedings under Section 11(b)(2) directed to Arknat and its subsidiaries and to petitioner.[8] In 1950, after abandoning an earlier proposal, Arknat filed a plan of reorganization under the Act,[9] and the proceedings on the plan were consolidated with the Section 11(b)(2) proceedings (App. 52a). Following amendment of the plan

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[7] *Cities Service Company*, 17 S.E.C. 5.

[8] *Arkansas Natural Gas Corporation et al.*, Holding Company Act Release No. 8842.

[9] The plan was filed under Section 11(e) of the Act. Under that section a registered holding company and its subsidiaries may submit a plan to the Commission to comply with Section 11(b) of the Act. The Commission is authorized to approve such a plan if it is found to be necessary to effectuate the provisions of Section 11(b) and fair and equitable to the persons affected, and, at the request of the company, the Commission may thereafter apply to a United States district court to enforce and carry out the provisions of a plan thus approved.

by petitioner and Arknat, the Commission in an order of October 1, 1952, approved the plan (App. 66a). The plan was ordered enforced by the United States District Court for the District of Delaware, and that decision was affirmed by the Court of Appeals for the Third Circuit.[10] The plan was subsequently consummated.

The plan provided for: (1) the retirement of Arknat's preferred stock; (2) the merger of Arkco into its parent, Arknat, with the latter's name changed to Fuel Oil; (3) the distribution by Arknat of the common stock of its subsidiary Arkla to the holders of its common stock and Class A stock;[11] (4) the conversion of both the common stock and Class A common stock of Arknat into a new common stock, on the basis of one-half new share for each old share outstanding; and (5) a cash payment aggregating $4,069,268.75 by petitioner to public holders of Arknat's common and Class A stock as a claims settlement (App. 52a-53a).

The Arknat Class A stock had had no vote; petitioner owned 24.3 percent of the 3,522,271 shares outstanding, with the remainder publicly held. The common stock carried all the voting power, and petitioner owned 75 percent of the 4,080,801 shares outstanding, with the balance publicly held. The plan thus substituted one-half a share of new common stock, which carried the sole voting power, for each share of Class

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[10] *Arkansas Natural Gas Corporation et al.*, Holding Company Act Release No. 11511 (October 1, 1952), approved and enforced, 109 F. Supp. 522 (D. Del.), affirmed 204 F. 2d 797 (C.A. 3) certiorari denied *sub nom. Public Common Stockholders Protective Committee* v. *Arkansas Natural Gas Corporation et al.*, 346 U.S. 865.

[11] Petitioner subsequently disposed of the interests in Arkla thus acquired.

A and common stock. As a consequence petitioner received 51.5 percent of the 3,801,536 shares of the new common stock and the other stockholders received 48.5 percent (App. 23a).

The Reservation of Jurisdiction

In the proceedings on the plan, a committee representing Class A stockholders of Arknat had objected to the plan on the ground that it continued and did not eliminate the public minority interest (App. 58a). In connection with this contention, the Commission, in considering whether the plan was an appropriate means for achieving results required by Section 11(b) of the Act, stated in its Findings and Opinion:

> We recognize that the continued existence of a minority interest in Fuel Oil presents a problem which may require corrective action. However, in view of the fact that Fuel Oil will remain under our jurisdiction as long as Cities is a registered holding company (a status which will continue until terminated by us), we believe that consideration of this problem may be deferred until a later date.
>
> * * * * *
>
> In view of the foregoing, we find that, *subject to the reservations noted*, the plan provides an appropriate means for achieving the results required by Section 11(b). [Emphasis added; App. 58a-59a.]

In its order the Commission specifically reserved jurisdiction with respect to:

c. The resolution of the problems presented by the continued existence of a minority public interest in Fuel Oil after consummation of the plan;

* * * * * *

e. The entaining of such further proceedings, entering of such further orders and the taking of such other action as may be necessary or appropriate to effectuate the provisions of Section 11(b) of the Act and as may be appropriate in connection with the plan, the transactions incident thereto and the consummation thereof. [App. 68a-69a.]

The Commission followed this course to permit effectuation of the many beneficial features of the plan without the delay that would be entailed in the resolution of the minority interest problem (App. 58a-59a).

Neither petitioner nor Fuel Oil filed a petition for rehearing with the Commission. At the request of petitioner and Fuel Oil, the Commission applied to the District Court to enforce and carry out the plan (App. 67a). Both companies supported the plan; they raised no objection to the reservation of jurisdiction. And the order of the District Court specifically provided for the enforcement of the plan "subject to the terms and conditions of said Order of the Commission."

The jurisdiction retained over Fuel Oil was reaffirmed in 1953 when Fuel Oil filed an application under Section 5(d) of the Act for an order declaring that it was no longer a holding company.[12] This order was entered

[12] Section 5(d) provides that the Commission may terminate the registration of a holding company which has ceased to be such, subject to such terms and conditions as are necessary for the protection of investors.

by the Commission only after Fuel Oil, without objection from petitioner, had supplemented its application with a consent that any order would be without prejudice to the jurisdiction previously reserved by the Commission. The order specifically provided that, with respect to the public minority interest question, Fuel Oil was to be considered a registered holding company.[13]

Petitioner's Exemption Application

On January 14, 1955, petitioner filed its applications for exemption. The Commission consolidated the proceedings on the application and the issue previously reserved in the Section 11 proceedings (App. 21a).

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[13] The order thus stated:

> The Commission finds that • • • [Fuel Oil] has ceased to be a holding company, that it is necessary for the protection of investors that the Commission retain jurisdiction over • • • [Fuel Oil] to the same extent as though it were still in all respects a registered holding company in respect of the matters over which jurisdiction was reserved in the Commission's Order dated October 1, 1952 • • • to the extent that the matters specified therein have not heretofore been disposed of, and that except for such retained jurisdiction the registration of • • • [Fuel Oil] as a holding company should cease to be in effect.
>
> It Is Therefore Ordered, pursuant to the provisions of Section 5(d) of the Act that • • • [Fuel Oil] has ceased to be a holding company and that, subject to the condition prescribed below, the registration of • • • [Fuel Oil] as a holding company shall cease to be in effect; provided, however, that this order shall be subject to the condition which is prescribed as necessary for the protection of investors that the Commission shall retain jurisdiction over • • • [Fuel Oil] in respect of any further proceedings, investigations or orders which the Commission may deem necessary or appropriate pursuant to the reservation of jurisdiction contained in the Commission's Order of October 1, 1952 • • • in the same manner and to the same extent as though • • • [Fuel Oil] were in all respects a registered holding company. [*Arkansas Fuel Oil Corporation*, Holding Company Act Release No. 12166 (October 7, 1953).]

For the first time, there was developed a detailed record of the relationships and dealings between petitioner and Fuel Oil.

On this record, the Commission found that Fuel Oil "has been assimilated into, and for all practical purposes is a part of the Cities oil and gas system" (App. 35a). It further found, referring to specific examples of transactions between petitioner and Fuel Oil, that

> * * * a conflict of interest manifests itself continuously between the Cities system on the one hand and Fuel Oil on the other, at least insofar as its impact on the minority stockholders of Fuel Oil is concerned * * * [App. 45a]

and that this conflict of interest which

> pervades all aspects of dealings between the Fuel Oil system and the Cities system is such that it constitutes a detriment to the interests of the minority stockholders, who are thereby deprived [of] a management conducting Fuel Oil's affairs with an eye single to its own advantage [App. 44a].

The Commission found that in these circumstances the public stockholders of Fuel Oil are disenfranchised as a practical matter (App. 46a).

These findings, as well as all other findings of fact made by the Commission, are not challenged by petitioner.

In affirming the Commission's order, the Court of Appeals agreed that there was ample support "in fact and common sense" for the conclusions of the Commission that as between Fuel Oil and the Cities system

there existed inherent conflicts of interest and that as a practical matter the public minority was disenfranchised (App. 18a). The court stated (App. 15a-16a):

> Because of the majority rule principle, the voting power of a permanent minority can easily be annulled. One reason why the minority is willing to run this risk is the belief that by and large, differences between majority and minority are differences over means rather than ends since the majority is as eager to further the interests of the corporation as the minority. * * * If the majority's basic concern is not for the welfare of the particular corporation but for an interest which may be adverse, there is no common interest and the minority is effectively disenfranchised—its votes are meaningless and it is at the mercy of the majority.[14]

The court held that, on the basis of the record, the Commission was justified in refusing to grant an exemption to petitioner until the minority interest was eliminated (App. 15a-16a).

ARGUMENT

Petitioner has tendered no question requiring review by this Court. The decision of the court below, affirming the Commission's order, is predicated essentially on a factual determination not disputed by petitioner. The decision, moreover, is clearly correct and does not conflict with prior determinations in this proceeding or with decisions of this Court.

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[14] The court found it unnecessary to determine whether a "complexity" also existed.

1. The Commission held that petitioner was not entitled to an exemption, which would have freed the companies involved from complying with Section 11(b)(2) of the Act, because in the circumstances there is a conflict of interest between petitioner and the public minority stockholders of Fuel Oil and because these stockholders are thereby disenfranchised as a practical matter (App. 18a). Petitioner does not challenge this finding of fact. It contends, however, (a) that the Commission is estopped from taking any action to cure this disenfranchisement, with its resulting unfair and inequitable distribution of voting power, because in 1952 the Commission approved the plan of reorganization of Arknat; (b) that the broad remedial provisions of Section 11(b)(2) do not reach this evil; and (c) that the Commission's decision conflicts with its determinations in other proceedings under Section 3(a). None of these contentions is valid.

(a). Petitioner's estoppel argument completely ignores the fact that it accepted the 1952 reservation of jurisdiction—a reservation, moreover, which was reaffirmed in the 1953 status order. Having enjoyed the benefits of the Arknat plan, it is petitioner, and not the Commission or the minority stockholder group, who is estopped. Had petitioner or Fuel Oil repudiated the jurisdiction reserved in the Commission's order, the Commission surely would not have made the necessary District Court application and the plan would have died a-borning.[15] On the other hand, if the Commission had found in 1952 that the plan had effected

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[15] See note 9, *supra*.

full compliance with Section 11(b)(2), as petitioner suggests (Pet. 13), the reservation of jurisdiction and the condition would have had no purpose.

In approving the 1952 plan, the Commission merely held that the absence of any voting power in the Class A stock of Arknat would be remedied by exchanging that stock for a voting security (App. 55a), leaving for later resolution under Section 11(b)(2) the minority interest problem (App. 58a-59a). This was done because of the desirability of permitting consummation of the many beneficial features of the plan, the third in a series of plans in proceedings spanning a four-year period. Section 11, because of the virtual impossibility of effecting full compliance in one omnibus plan, has been consistently administered so as to permit compliance in a series of plans. *Phillips* v. *Securities & Exchange Commission*, 156 F. 2d 606, 609 (C.A. 2). This technique for effecting compliance may not be used, however, as a means of frustrating the achievement of the objectives of Section 11. Before a registered holding company is released from the operation of the statute, it must be purged of those abuses encompassed by Section 11(b)(2). The fact that Fuel Oil (Arknat with its name changed) is no longer in the utility business and Cities is no longer in the domestic utility business is a circumstance stemming from a sequence of steps taken to comply with the statute and does not affect the extent of compliance which must be achieved.[16]

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[16] "It is not the order of consummation of steps in its plan to cease to be a holding company which has major significance." *In re The United Corporation*, 128 F. Supp. 725, 738 (D. Del.), affirmed, 232 F. 2d 601, 605-606 (C.A. 3), certiorari denied, 352 U.S. 839.

(b). Section 11 of the Act has been described as the "very heart of the title".[17] Section 11(b)(2) is a remedial provision designed to simplify corporate structures of registered holding company systems, to provide investors with securities in these simplified structures that carry meaningful rights, and to afford investors protection from abuse. That section requires the Commission to order each registered holding company, and each subsidiary company thereof, to take such steps as the Commission shall find necessary

> to ensure that the corporate structure or continued existence of any company in the holding-company system does not unduly or unnecessarily complicate the structure, or unfairly or inequitably distribute voting power among security holders, of such holding-company system. [App. 72a.]

Any element of system corporate structure, or the continued existence of any company in the system, which creates a "complexity" or an inequitable distribution of voting power among security holders in the system, falls within the statutory proscription. This is clear from the language of Section 11(b)(2) itself and also from Section 11(a)—a guide giving "meaningful content" to the terms of the latter section[18]—which imposes a duty upon the Commission in connection with its functions under Section 11(b) to examine "the relationships among the companies in the holding-company system * * * and the character of the interests thereof * * *."

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[17] *North American Company* v. *Securities & Exchange Commission*, 327 U.S. 686, 704, note 14.

[18] *American Power & Light Company* v. *Securities & Exchange Commission*, 329 U.S. 90, 104.

Under any criterion, corporate structure in a holding company system includes a public minority interest in a subsidiary. This is not disputed by petitioner, which shows in its published financial statements the minority interest in Fuel Oil, in accordance with accepted accounting principles, as a specifically designated item in the corporate structur of the Cities system.[19] The Commission examined this aspect of the corporate structure in the context of the operating relationships of the companies and found that its existence produced, in the corporate structure of the Cities holding company system, a "complexity" and an inequitable distribution of voting power (App. 46a). The Commission made " * * * an informed, expert judgment on the problem." *Securities & Exchange Commission* v. *Chenery Corp.*, 332 U.S. 194, 207.

The Commission observed that its "experience has disclosed that where exigencies of the situation are sufficiently compelling the management has little choice but to make decisions in the light of the over-all needs of the system, whatever the effect on the minority holders of securities. In such a situation the right to

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[19] Under accepted accounting principles, the minority interest is required to be shown separately in a consolidated balance sheet. That interest is set forth between the liabilities and net worth sections, with separate amounts shown for minority interests in the capital stock and surplus. Securities and Exchange Commission Regulation S-X, Rule 4-07, Securities and Exchange Commission Accounting Series Release No. 7, at page 9 (1938); Greidinger, *Preparation and Certification of Financial Statements*, 156 (1950); Kennedy and McMullen, *Financial Statements*, 393 (1952); Lewis, *Consolidated Statements*, 46-54 (1942); Nixon and Kell, Editors, *Accountants' Hand Book*, 4th ed., 238 (1956). The latter states: "The holding of shares of stock by persons with an interest in only one of the affiliated companies gives rise to a conflict between the dominant controlling interests and the minority interest which is reflected in the problem of preparing a consolidated statement."

vote for directors is an illusory protection to the minority stockholders where the bulk of the voting stock is system held." (App. 33a, quoting from *Alabama Power Company*, 34 S.E.C. 219, 225 (1952)). The vice here is not *per se* in majority rule, as petitioner intimates (Pet. 20), but rule by a majority which has interests that conflict with those of Fuel Oil; the public stockholders of Fuel Oil are entitled to a management that will conduct its affairs with an eye single to its own advantage. If Fuel Oil's twenty thousand public minority shareholders had their stock interest and accompanying vote at the Cities level instead of at the Fuel Oil level, then they would have a voice in the election of the directors who actually make the decisions for the entire Cities system, including Fuel Oil. And, with the conflict of interest thus eliminated, the decisions made for the benefit of the system as a whole would benefit all the security holders of Cities, including those now holding the minority interest in Fuel Oil.[20]

Petitioner argues, however, that Fuel Oil—although it concededly is a registered holding company—is not a "holding company" under the third sentence of Section 11(b)(2) (Pet. 11). The third sentence provides:

> Except for the purpose of fairly and equitably distributing voting power among the security holders of such company, nothing in this paragraph shall authorize the Commission to require any change in the corporate structure or existence of any company which is not a holding company, or of any

[20] In addition to this defect in "the corporate structure" of the Cities system, the "continued existence" in the Cities system of Fuel Oil with a public minority interest, which results in an unfair and inequitable distribution of voting power, may not be permitted under Section 11 (b) (2) in the Commission's view.

> company whose principal business is that of a public-utility company. [App. 72a.]

The limitation imposed by the foregoing sentence has no relevance where, as here, the Commission action is "for the purpose of fairly and equitably distributing voting power among the security holders of such company"—namely, Fuel Oil. The third sentence only restricts Commission action directed to a "complexity." Moreover, petitioner's argument is predicated on the unacceptable proposition that the Commission has less power over a registered holding company, the primary object of regulation, than over other companies subject to Section 11(b)(2)—a view wholly at variance with the entire scheme of the Act.[21] Furthermore, because of the Commission's reservation of jurisdiction made in 1952 and reaffirmed by the condition imposed in 1953, Fuel Oil for purposes of this proceeding must be viewed, as it was in 1952, as a registered holding company with a utility subsidiary, *i.e.*, a holding company.[22]

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[21] In *In re The United Corporation*, *supra*, 232 F. 2d at 606, note 11, the court pointed out that "[o]nce a company becomes a *registered holding company*, it remains such until the Commission orders otherwise * * * even though it is no longer *a holding company*," and as a registered holding company cannot evade the statute's command merely because it has, in the process of compliance with the statute, disposed of its utility interests.

[22] Petitioner now contends, for the first time, that the Commission may not invoke Section 11(b)(2) in the instant case because under Sections 12 and 13 of the Act the Commission may regulate all business dealings, including contractual dealings, between or among a holding company or any of its subsidiaries (Pet. 12). Even if this argument were valid, it would afford no basis for granting an exemption to Cities. On the contrary, it would be all the more reason for denying an exemption which would relieve the Cities system from Commission regulation under those sections. Moreover, Sections 12 and 13 are not a substitute for the explicit

(c). The conclusion reached by the Commission is consistent with applicable precedents. In every proceeding in which it has addressed itself to the problem, the Commission has uniformly found a violation of Section 11(b)(2) in circumstances similar to those existing in the instant case.[23]

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mandate of Section 11(b)(2), requiring the Commission to direct the elimination of an inequitable distribution of voting power. And even if these sections are viewed as providing alternative remedies, it is properly within the province of the Commission to determine which is the more satisfactory. See *Securities & Exchange Commission* v. *Chenery Corp.*, 332 U.S. 194, 209; see also *American Power & Light Co.* v. *Securities & Exchange Commission*, 329 U.S. 90, 112-113.

[23] See, *e.g.*, *Sioux City Gas and Electric Company*, 30 S.E.C. 5, 14 (1949), approved and enforced N.S. Iowa, Civil Action No. 571 (1949); *The Southern Co.*, 31 S.E.C. 821, 834 (1950); *The United Gas Improvement Company*, 33 S.E.C. 729, 738 (1952); *Alabama Power Company*, 34 S.E.C. 219, 224-225 (1952); *Southern Natural Gas Co.*, 34 S.E.C. 718, 726 (1953); *Union Electric Company of Missouri*, 35 S.E.C. 483, 494 (1953). See also *Georgia Power and Light Company*, 18 S.E.C. 89 (1945), enforced N. D. Georgia, Civil Action No. 133 (1945); *Pennsylvania Edison Co.*, 23 S.E.C. 148, 157 (1946); *Electric Power & Light Corp.*, 29 S.E.C. 52, 65 (1949); *New England Electric System*, 32 S.E.C. 215, 217 (1951).

Occasions have arisen where a public minority interest was permitted to be created only upon the understanding that it would be eliminated. See, *e.g.*, *Ohio Edison Company*, 30 S.E.C. 613, 622-623 (1949), 31 S.E.C. 272, 285 (1950); *Central Louisiana Electric Company, Inc.*, 32 S.E.C. 266, 282 (1951), 32 S.E.C. 743 (1951).

Petitioner's characterization of these cases as involving "voluntary" plans is misleading and erroneous. Congress intended that the requirements of Section 11 should be mandatory upon the companies affected independent of the institution of proceedings by the Commission, and "voluntary" action taken under Section 11(e) to comply with the requirements of Section 11(b) is prompted by the certain knowledge that involuntary proceedings will otherwise be instituted. *Consolidated Electric & Gas Co.*, 55 F. Supp. 211, 216 (D. Del.); *Public Service Commission* v. *Securities & Exchange Commission*, 166 F. 2d 784, 787 (C.A. 2), certiorari denied, 334 U.S. 838. Indeed, certain of the "voluntary" plans were consolidated with Section 11(b)(2) proceedings that the Commission had already begun.

Petitioner complains that the Commission has granted exemptions under Section 3(a) where there was a public minority interest (Pet. 15-18). In its indiscriminate collection of cases, petitioner demonstrates its misconception of the view of the Commission, and also of the court below, as to a public minority interest. Such an interest does not *per se* bar an exemption. The exemption is foreclosed only where the public minority interest exists in a situation which gives rise to a conflict of interest in circumstances such as those existing in the instant case.[21]

Furthermore, petitioner reads Section 3(a)(5) as if it were intended to be an escape hatch to relieve it from complying with Section 11(b)(2). In its whole approach to the exemption question and its attack on the Commission's determination, petitioner ignores altogether the fact that regulation of its system began when it was a vast hybrid system, and that elimination

[21] Certain of the cases referred to by petitioner were cited by it in the administrative proceedings, and the Commission pointed out (App. 34a-35a) that "the question whether the presence of a minority interest involves a detriment which the statute seeks to prevent must, of course, be resolved on the facts in each case", and then addressed itself specifically, among others, to the two cases emphasized by petitioner in its petition, namely, *Electric Bond & Share Company*, Holding Company Act Release No. 11675 (1953), and *Standard Oil Company*, 15 S.E.C. 373 (1944). As to the former, the Commission pointed out that it was "satisfied that elimination of the minority interest was not required where, among other things, the intra-system transactions, which consisted exclusively of a servicing arrangement, were to be performed at cost." As to the *Standard Oil* case, it observed that "the minority interest did not exist, as it does here, in a registered holding company to which Section 11(b)(2) proceedings had been directed", noting that in "the context of a system which meets the conditions for exemption under Section 3(a) of the Act we have not invoked the 'unless and except' clause to reach all parts of the system but have generally confined remedial action under Section 11(b)(2) to the holding company."

of the public minority interest is simply the last step in a reorganization of a registered holding company—*not* a sudden Commission effort to begin regulation of an oil enterprise that never had extensive utility interests and is only technically a registered holding company because of a minor foreign utility holding. "The problem arises out of the unraveling and reorganization of [a] vast empire * * * pursuant to the command of the Act." *Securities & Exchange Commission* v. *Drexel & Co.*, 348 U.S. 341, 342.

2. Petitioner also contends that the decision below conflicts with decisions of this Court and the policy of the Interstate Commerce Act.

Comstock v. *Group of Investors*, 335 U.S. 211, chiefly relied upon by petitioner (Pet. 19-21), is inapposite. This Court held in that case, which arose under Section 77 of the Bankruptcy Act, that a claim of a parent against the subsidiary's estate would not be subordinated merely because of the control relationship, in the absence of a showing of bad faith. In the instant case, public stockholders of Fuel Oil would be subject to the same burden if they asserted claims against Cities, as was the case in *In re American & Foreign Power Co.*, 80 F. Supp. 514 (D. Maine), where the court enforced a plan approved by the Commission which provided for settlement of claims against a holding company. Section 11(b)(2), however, is a prophylactic provision intended to prevent abuses before they occurred so that investors would not be forced to resort to the unhappy alternative of litigation to protect their interests.[25]

[25] In fact, there is presently pending in the Delaware Chancery Court an action by Fuel Oil stockholders arising out of the intercompany activities. *Auerbach* v. *Cities Service Co. et al.*, Del Ch. Civ. No. 690.

The short answer to petitioner's argument (Pet. 21) as to the permissibility of a minority interest under the Interstate Commerce Act, assuming its accuracy, is that Congress embodied a different policy in the Public Utility Holding Company Act where a public minority interest results in an inequitable distribution of voting power or a complexity.[26]

3. There are nine registered holding company systems, other than petitioner, which have public minority common stock interests in subsidiaries.[27] Petitioner asserts that the decisions below will have a direct effect on each of these companies (Pet. 19). The extent to which elimination of these interests would be required under Section 11(b)(2) would, as already pointed out (*supra*, p. 19), depend upon the circumstances in each case, especially the degree of actual or potential conflict of interest. These are matters which the Commission has not yet determined.

[26] In *Schwabacher* v. *United States*, 334 U.S. 182, cited by petitioner (Pet. 21), there would be no minority interest in the surviving company following consummation of the merger there involved. The only question there presented was whether the participation of minority stockholders in a merger was to be determined by the Interstate Commerce Commission or by the courts under the state law.

[27] The situations involving publicly held preferred stock interests in subsidiaries are irrelevant because the income participation of these stockholders is fixed by their contractual dividend rate so that generally there is not the conflict of interest which may motivate a parent to treat a subsidiary with a minority public common stock interest in a manner which will produce the most income for the parent.

CONCLUSION

For the reasons stated, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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